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Wheat Update

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Report Highlights:

Estimates of how much wheat Brazil will need to import in the next few months from non-Mercosul sources range from 700,000- 1.5 million metric tons (mmt). The Brazilian wheat industry is currently lobbying the government for a temporary elimination of the import tax. In setting the new minimum price for wheat, the GOB provided incentives to farmers to produce better-quality wheat .

General Information:

Supply Situation

Estimates of how much wheat Brazil will need to import in the next few months from non-Mercosul sources range from 700,000- 1.5 million metric tons (mmt). Those on the low end of this range cite the historical tendency for people to declare a lack of wheat in Argentina, only then to find Argentine farmers exporting wheat out of the bags sitting in their fields when the price is attractive enough. In addition, imports from Mercosul members Paraguay and Uruguay are expected to reach 800,000 tons, well above the forecasted 500,000 tons. While industry sources have praised the

quality of this year's Uruguayan crop, noting that it is similar to Argentine, they note that Paraguay has a reputation of producing an inconsistent product. This year industry reported that Paraguayan wheat is dark, making it less attractive.

Looking forward to 2010, industry sources again foresee imports from non-Mercosul origins. Since Argentina, Brazil's main supplier, continues to have policy uncertainties that negatively affect cropping choices, productivity and export competitiveness. Given the expected drop in planted area and yields in Argentina because of a further shift toward soybeans as a result of government intervention in wheat markets and farmers' fragile financial situations and lack of credit, Argentina may once again limit exports. Even with continued exports from Uruguay and Paraguay and another large domestic crop, Brazil is expected to import about 500-700,000 tons of non-Mercosul wheat the next crop year.

Brazil's 2008/2009 wheat planted area is expected to remain flat or increase slightly, with production estimates ranging from 5.5-6.1 mmt. Financing does not appear to be an issue. The state governments are working in partnership with the Bank of Brazil to ensure funding. Another factor supporting wheat planting is that most wheat producers are primarily soybean producers who will plant more wheat to prepare the land for soybeans as soybean production continues to expand. In addition, the government's minimum prices (discussed in further detail below) should spur or at least maintain production. Moreover, the cost of crop insurance will be borne in part by the government - with the federal government contributing 70% of the crop insurance cost and the state government contributing 15%. However, in spite of these incentives, Brazilian production is difficult to forecast since crop yields vary greatly because of significant weather challenges throughout the wheat production cycle- dryness during planting, frost mid-season and rains during harvest. For example, right now, the dry April weather in Parana has not been good for wheat plantings.

Author Defined:

Potential Suppliers

Brazil likely will seek non-Mercosul wheat from the United States, Canada, and Russia. Canada and the United States are well-situated to be the main suppliers. The Canadians are very aggressive this year given that its crop in 2008 was quite large and of high quality. Industry sources noted rates as low as \$245-\$270/CNF (market prices are closer to \$265-275).

Discussion of bartering imported Russian wheat for Brazilian pork continues in spite of little enthusiasm from the wheat industry due partly to quality issues. This year there have been reports of a high presence of the sunn pest, also known as the Russian wheat bug which emits an enzyme that dissolves gluten in developing wheat. The result is that bread dough breaks down after about

an hour.

Common External Tariff

Wheat sourced from outside Mercosul must pay the 10 percent Common External Tariff (CET). It is estimated that the CET is costs about \$25/ton. The Brazilian wheat industry is currently lobbying the government for a temporary elimination of the CET. The Minister of Agriculture has stated that if the tariff is to be lifted temporarily, it is crucial for this exemption to be at the right moment and in the right quantity, so that imported wheat will not lead to a reduction in the price paid to Brazilian wheat farmers. To that extent, the CET should be reduced only when inventories are nearing depletion, and in a volume that will keep the market supplied until shortly after the next harvest. It is expected that the inventories of domestic wheat will be sold in May and June, and, if the exemption is granted, shipments would likely occur in July and August. Several buyers expressed concern that if they wait until July or August to purchase wheat, they could get stuck with expensive wheat; since prices usually drop if there is a large domestic crop harvested starting in September.

Minimum Price

In setting the new minimum price for wheat, the GOB provided incentives to farmers to produce better-quality wheat. The National Monetary Council, on March 26th, readjusted by greater percentages for melhodor (wheat with baking qualities which will increase the quality of soft wheat when its blended for milling purposes) and bread wheat which is considered to be of better quality and is used for bread making. The minimum prices for the two types, which used to be R\$480 (US\$ 214) per ton, have increased, respectively, by 15.63% and 10.42%, rising to R\$530 (US\$ 237) and R\$555 (US\$ 248) per ton. In contrast, the minimum price for soft wheat increased only 5.54%-to R\$440 (US\$196.43) from R\$417 (US\$186.16).

While industry observers see this as a step in the right direction, they are divided as to whether this regime will reduce production of low-quality wheat. Some observers are optimistic and think that within 3-5 years there may be significant changes in the class of wheat grown in Rio Grande do Sul—the region which currently produces predominately low quality wheat. Others note that producers are reluctant to make changes and the minimum price is still sufficient especially in that the wheat producers are also soybean producers who have had a profitable year. In addition, this new regime will require cooperatives to segregate wheat. In the past, the industry has not embraced the idea of wheat classification due to the increased costs of segregated warehouses.

Selected 2008/09 Minimum Prices for Wheat

Type	Unit	2008/2009 Price (R\$/unit)	2008/2007 Price (R\$/unit)	Percentage Increase
Melhorador*,durum	mt	R\$550	R\$480	15.63%
Bread, type 1	mt	R\$530	R\$530	10.42%
Soft	mt	R\$440	R\$417	5.54%

*wheat with baking qualities which will increase the quality of soft wheat, when its blended for milling purposes